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RUEHUL/AMEMBASSY SEOUL 9383
RUEHGP/AMEMBASSY SINGAPORE 7230
RUEHKO/AMEMBASSY TOKYO 9639
RUEHML/AMEMBASSY MANILA 0361
RUEHJA/AMEMBASSY JAKARTA 4267
RUEHKL/AMEMBASSY KUALA LUMPUR 3942
RUEHHI/AMEMBASSY HANOI 3527
RUEHBY/AMEMBASSY CANBERRA 4807
RUEHWL/AMEMBASSY WELLINGTON 2073
RUEHHK/AMCONSUL HONG KONG 9159
RUEHGH/AMCONSUL SHANGHAI 1801
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SIPDIS

SIPDIS

STATE PLEASE PASS USTR
STATE FOR EAP/RSP/TC, EAP/EP
USTR FOR KATZ AND STRATFORD
USDOC FOR 3132/USFCS/OIO/EAP
TREASURY FOR OASIA/TTYANG AND HAARSAGER
TREASURY ALSO PASS TO FEDERAL RESERVE/BOARD OF
GOVERNORS, SAN FRANCISCO FRB/TERESA CURRAN, AND NEW YORK FRB MARI
BOLIS

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TAGS: [EINV](#) [EFIN](#) [ECON](#) [SENV](#) [TW](#)

SUBJECT: Taipei Economic Brief for February 2008

¶1. (U) Summary. Following are the highlights of February 2008 economic events in Taiwan: Better-than-expected export performance prompted upward adjustment of economic growth in 2007.... Forecasters anticipate economic slowdown in 2008.... Economic performance in January remained strong despite heavy inflationary pressure.... Private investment exceeds 2007 goal.... Industrial park renewals with low land costs are designed to accommodate returning Taiwan firms.... Earnings by science industrial park based firms increase.... Taiwan's tourism potential highlighted.... Tax reform program introduced three weeks before the presidential election.... Multinational corporations to set up training and R&D facilities.... Waste recycling industry grows.... END SUMMARY.

2007 Economic Growth Adjusted Upward

¶2. (U) Better-than-expected trade performance in the fourth quarter (Q4) of 2007 prompted forecasters to revise Taiwan's 2007 economic growth rate upward. Taiwan's exports in Q4 posted a year-on-year growth of 15%, higher than the 9% projected in November 2007 by the Directorate General of Budget, Accounting and Statistics (DGBAS). Taiwan's trade surplus in the quarter, therefore, set a new high of US\$10 billion, 27% more than forecast. In response, in late February, DGBAS raised Taiwan's real GDP growth for Q4 to 6.4%, overall 2007 economic growth from 5.4% to 5.7%. The private Taiwan Institute of Economic Research (TIER) also raised Taiwan's estimated 2007 economic growth to 5.1% from the 4.4% it forecast in November ¶2007.

Economic Slowdown Projected for 2008

¶3. (U) Both DGBAS and TIER expect the U.S. sub-prime mortgage problem will dampen growth in developed economies which, in turn, will adversely affect the performance of Taiwan's export-oriented economy in 2008. According to DGBAS, export growth will slow from 10% in 2007 to 6% in 2008, and real GDP growth will decline to

barely above 4%, although private consumption will grow faster in 2008 as businesses distribute dividends to their shareholders.

Performance in January Remains Healthy

¶4. (U) Taiwan's economy, nevertheless, continued to perform well in January 2008. Export value grew 12% year-on-year to US\$22.14 billion, mainly driven by stronger demand from Taiwan's Asian neighbors, where many Taiwan exporters have located their production bases. Strong foreign demand remained in January, manifested by 17% growth in export orders. Double-digit manufacturing growth spilled over from the second half of 2007 to January 2008. The unemployment rate in January 2008 declined to an 11-month low of 3.8%.

Import-Driven Inflation

¶5. (U) Higher energy, grain, and basic metal costs, which contributed to 15% import growth, fueled inflationary pressure in January as Taiwan's consumer price index rose at a year-on-year rate of 3%. The wholesale price index in January 2008 increased 10.2% year-on-year, the highest rate since November 2004. Higher oil prices caused the January import price index to surge to an 18-year high of 16.94%. Crude oil import costs in January averaged US\$88 per barrel, up 70% from January 2007.

¶6. (U) With higher import costs likely to persist, local forecasters predict inflation will stay at almost 3% during the first half of the year, even though money supply leveled off in January. To stabilize prices, Taiwan authorities will reduce the 5% business transaction tax on imported grains and grain products, in addition to the freeze in gasoline prices implemented in January.

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Private Investment Exceeds MOEA's 2007 Goal

¶7. (U) Private investment figures in 2007 surpassed targets set by the Ministry of Economic Affairs (MOEA). According to the MOEA's Cooperative Office for Investment Promotion (COIP), investment in private projects completed in 2007 totaled NT\$1.17 trillion (US\$37.3 billion), surpassing the MOEA-set target of NT\$900 billion (US\$28.6 billion) by 30%. There were 1,466 new private projects launched in 2007, the investment value of which was NT\$1.65 trillion (US\$52.4 billion), exceeding the MOEA's target of NT\$1.1 trillion (US\$35.2 billion) by 50%. The MOEA's 2008 new private investment target is NT\$1.77 trillion (US\$56 billion), up 7.3% from 2007.

Industrial Park Renewal Program

¶8. (U) The Executive Yuan recently approved a 2008-2010 "Industrial Park Renewal Demonstration Plan." Initially, two old unused industrial parks will be renovated, and the plan will eventually be expanded to cover all aging industrial parks. Demand for industrial land has been strong due both to the expansion of science parks, and to a growing number of returning Taishangs (Taiwanese companies abroad), many of which are manufacturers in traditional industries. According to the Industrial Development Bureau (IDB), nearly half of Taiwan's industrial parks are over 30 years old and lack sufficient infrastructure.

Additional Funding for Industrial Land Program

¶9. (U) The Executive Yuan approved an additional NT\$20 billion (US\$625 million) for the '006688' program, which provides businesses with industrial land for lease at discounted rates. The program aims to encourage Taishangs abroad to invest in Taiwan. The funds will be available through December 31. The Industrial Development Bureau expects the program to attract 300 manufacturing plants to invest NT\$106 billion (US\$3.3 billion) in Taiwan's industrial parks, create NT\$120 billion (US\$3.75 billion) in production, and increase tax revenue by NT\$1.8 billion (US\$56 million). Under the program, industrial land will be rent-free for the first two years, discounted by 40% in the next two years, and discounted by 20% for the fifth and sixth years.

Taishangs Returning Home

¶10. (U) A growing number of Taishangs are returning to Taiwan, mostly from China, where legal changes have resulted in relatively less positive investment climate for some Taiwan firms. Labor, land, and utilities costs in China have risen and drastically narrowed the gap with Taiwan. The PRC has also reduced or eliminated some tax incentives for foreign investors. According to Taiwan's Department of Investment Services (DOIS), over the past year, 102 Taishangs have expressed interest in returning to Taiwan, and many of them have returned in clusters. Ten bolt and nut manufacturers in China, for example, have located their plants at the Gangshan Benjhou Industrial Park in Kaohsiung County. PCB manufacturer Unitech and Process Advance Technology Ltd. have set up factories at the Litze Industrial Park in Ilan. The recently opened Kaohsiung Software Science-based Industrial Park has accommodated ten returning companies. Cheng Shin Rubber Inc. Co., the largest tire supplier in China and 12th-largest tire supplier in the world, will invest NT\$15 billion (US\$461.5 million) in Taiwan. A number of Taishangs who maintain operations in China prefer to remain low-key about their investment in Taiwan to avoid any potential repercussions in the PRC.

¶11. (U) When delivering a keynote speech to the Taiwan business community's Lunar New Year Party in late February, President Chen Shui-bian announced that he plans to grant amnesty to Taiwan

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business firms illegally investing in China because these firms are suffering from a deteriorating investment environment in China. Minister of Economic Affairs Steve Chen has outlined the following assistance to Taishangs in China:

- setting up a Taiwan firms service office in July 2006;
- encouraging Taiwan firms to return to Taiwan through industrial land rental waivers and discount programs;
- offering sufficient financing;
- reducing the tax burdens on foreign expatriates employed in Taiwan;
- relaxing restrictions on employment of foreign blue-collar workers;
- providing Taishangs with capital for investment in Latin America; and
- planning to lower the corporate income tax from 20% to 17.5%, verse the PRC's 25%.

Science Industrial Parks

¶12. (U) In 2007, the sales revenue of business firms in Taiwan's science industrial parks grew 12.3% from 2006 to a new high of NT\$1,966.4 billion (US\$60.5 billion). The number of business firms in science industrial parks as of December 2007 totaled 686, up 6% from 2006. The workforce in the science industrial parks grew 10.5% to 201,608 persons.

Taiwan: 30th in Tourism

¶13. (U) In its 2007 Travel and Tourism Competition Report, the World Economic Forum (WEF) ranked Taiwan the 30th-best tourism destination of 124 economies surveyed, and fourth in Asia. With further development, Taiwan will become an "important tourism destination" for overseas tourists. In terms of human, natural, and cultural resources, Taiwan ranked second in Asia and 23rd in the world because of destinations, such as Taroko Gorge, Sun Moon Lake, and the National Palace Museum. Taiwan's tourism promotion efforts have paid off. Following growth of 4.2% in 2006, the number of inbound passengers in 2007 rose 5.6% to a new high of 3.7 million. This led to a 10% increase in 2007 tourism revenue to US\$38 billion, according to a survey by the World Tourism and Travel Council (WTTC).

Tax Reform

¶14. (U) In mid-February, the Executive Yuan (EY) approved a tax reform proposal submitted by the Ministry of Finance (MOF). The proposal requires Legislative Yuan approval. The EY will phase out tax incentives offered by the Statute for Industrial Upgrading (SIU), which will expire at the end of December 2009. The phase-out of all tax incentives will increase the annual tax revenue by NT\$148 billion (US\$4.6 billion). The EY will use the increased revenue to

make up losses arising from the planned tax cuts, which are estimated to cost NT\$150 billion (US\$4.7 billion). For corporate income, the 10% tax on retained earnings will be dropped and the corporate income tax will be reduced from 25% to 17.5%. For personal income, the tax rates will be lowered from 6-40% to 5.5-37.5%. The across-the-board deductible will increase from NT\$46,000 to NT\$60,000 (US\$1,875) per unmarried taxpayer and from NT\$92,000 to NT\$120,000 (US\$3,758) per couple. In addition, the deductible for each wage earner will increase from NT\$78,000 to NT\$100,000 (US\$3,125), the deductible for a disabled person will increase from NT\$77,000 to NT\$100,000 (US\$3,125), and the deductible for education will increase from NT\$25,000 per household to NT\$25,000 (US\$781) per student.

Biotechnology Training Center

¶15. (U) Merck Group, a German pharmaceutical and chemical conglomerate (not directly related to the U.S. pharmaceutical firm

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of the same name), and Taiwan's state-owned Development Center for Biotechnology (DCB) will set up the Asia Technology Training Center (ATTC) joint venture. Through the joint venture, Merck will develop a platform for protein-based drugs by promoting its manufacturing processes in the Asian market. ATTC is Merck's first training center in the Asia-Pacific region, and third in the world, with the other two located in the United States and Germany. ATTC will be located in the DCB compound in Taipei County. DCB will provide manpower and logistic resources, while Merck will supply systems, lab technicians, and a technical manager to handle clients in Asia. Initial investment in the project will be a modest NT\$10 million (US\$312,500). Improved manufacturing processes for protein-based drugs, nevertheless, will generate annual revenue of US\$100 million, according to Merck. The ATTC will benefit small pharmaceutical firms by providing top-notch consulting services for the production of protein-based drugs.

HP to expand R&D center in Taiwan

¶16. (U) HP, the world's largest personal computer (PC) supplier, will expand its Product Development Center (PDC) in Taiwan by doubling the size of the PDC's workforce. This will make the Taiwan PDC the largest among HP's R&D centers in the world. The center will add 600 new employees by the end of this year. HP's PDC in Taiwan started with only 24 employees in 2002. The Taiwan PDC offers a number of advantages, including relatively low R&D costs and proximity to Taiwan's original design manufacturers (ODMs) of PCs and handheld devices, which will improve HP communications efficiency. With its focus on notebook computers over the past five years, HP's PDC in Taiwan has developed 50 product lines for 100 different specifications, including its first MCE (multimedia center edition) notebook computer. In 2008, software will be an area of focus for HP Taiwan. The company's global software business revenues grew by 306% in 2007. According to the Ministry of Economic Affairs, HP maintained its position as the world's top seller of notebook computers, shipping 23.3 million units worldwide in 2007, up 58% from 2006.

Sony Computer Entertainment to Establish R&D Center

¶17. (U) Sony Computer Entertainment (SCE) has signed a letter of intent with the Ministry of Economic Affairs (MOEA) to develop digital media. Under this arrangement, SCE will set up an R&D center and offer game development training in Taiwan. SCE will cooperate with Taiwan educational organizations to implement training programs, which will be aimed at college/university students. Lecturers will include SCE's own gaming R&D experts, as well as leading game developers in Japan. The ultimate goal is to build Taiwan's capability to produce universal, world-class game software.

Vestas to Form Wind Power Subsidiary in Taiwan

¶18. (U) Vestas Wind Systems A/S of Denmark announced it will form a subsidiary in Taiwan. Vestas, one of the major wind turbine suppliers in Taiwan, accounts for over 30% of the global wind power

market and 70% of the offshore wind turbines market. Vestas has supplied Taiwan with over 70 wind turbines, and its major customers is the state-owned Taiwan Power Company, which has built several wind generators in Yunlin County. Vestas' potential customers include Aerospace Industrial Development Corporation and Star Electric Power Corporation. Meanwhile, Vestas will be an important source of technologies for Taiwan's wind turbine component manufacturers, including TECO Electrical Engineering. Under Taiwan's long-term wind power development plan launched in 2001, TPC will build 200 wind turbines in three stages, at an estimated cost of NT\$100 million (US\$3.1 million) to NT\$150 million (US\$4.7

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million) for each stage.

Solar-Power Generation Program

19. (U) On February 1, the state-owned Taiwan Power Company (TPC) announced a NT\$3.57 billion (US\$110 million) solar-power generation program. Under the program, TPC will build solar-power generators to provide electricity to local authorities and primary/middle schools. Each generator will have a capacity of 1,000 kwh, and the annual power generated under the program will reach 12.5 million kw, which will reduce carbon dioxide emissions by 7,750 tons.

Industrial Wastes Recycling

20. (U) Taiwan began to promote recycling of industrial wastes in 2001. The number of industrial waste recycling firms increased from 305 in 2002 to 915 in 2007. The amount of industrial waste recycled surged from 8.04 million tons in 2002 to 11.82 million tons in 2007, and the output value grew from NT\$24.9 billion (US\$778 million) to NT\$42 billion (US\$1.3 billion) during the same period.

YOUNG